

# Presentation to Parliament Standing Committee on Finance

15 October 2014



South African Reserve Bank

## Scope of the report

- The report covers the Bank's mandate and purpose
- Strategic focus areas and the performance review against the objectives
- The annual monetary policy report, as required by the SARB Act
- Details on the governance structures
- Group annual financial statements – 2013/14

# Overall background & highlights

- **Integrated Reporting**

- The Bank has been gradually moving towards full integrated reporting in line with best practice and international guidelines over the past few years
- This year the report has been well received for its easy accessibility and transparency and revised design and content
- Going forward the Bank will be improving on this base and its disclosures in terms of sustainability



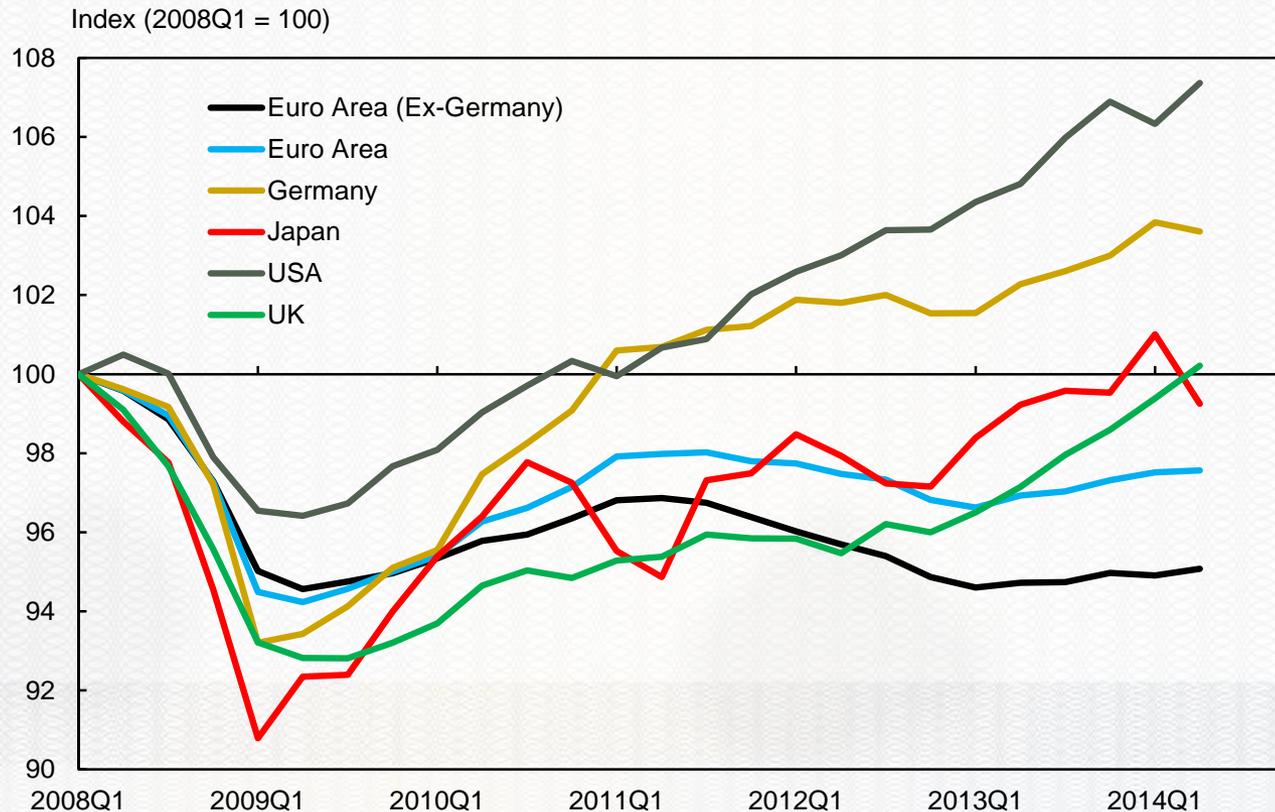
# Strategic Focus

- Execution of the Bank's mandate - price stability and explicit financial stability responsibility
- Implementing the Twin Peaks Regulatory Model in order to streamline the financial regulatory architecture
- Contribute to sound global central banking
- Enhance the Bank's reputation as a respected partner and institution in the domestic economic environment
- Enhance organisational effectiveness and efficiency through investment in people
- Incorporate and more closely align the subsidiaries in a comprehensive group structure

# Economic developments and Outlook

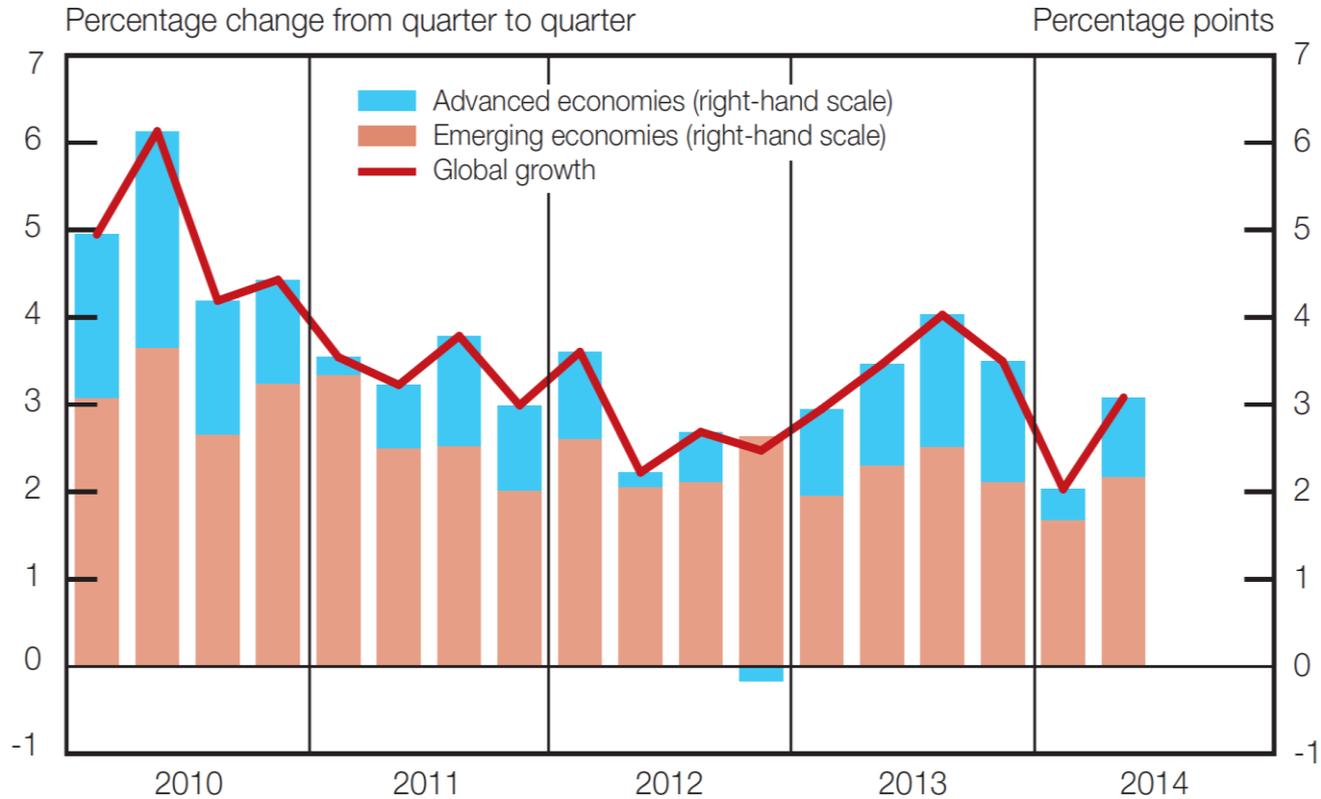


# Global growth appears to be recovering, with differing pace of recovery in advanced economies.....



# but there are risks to the outlook....

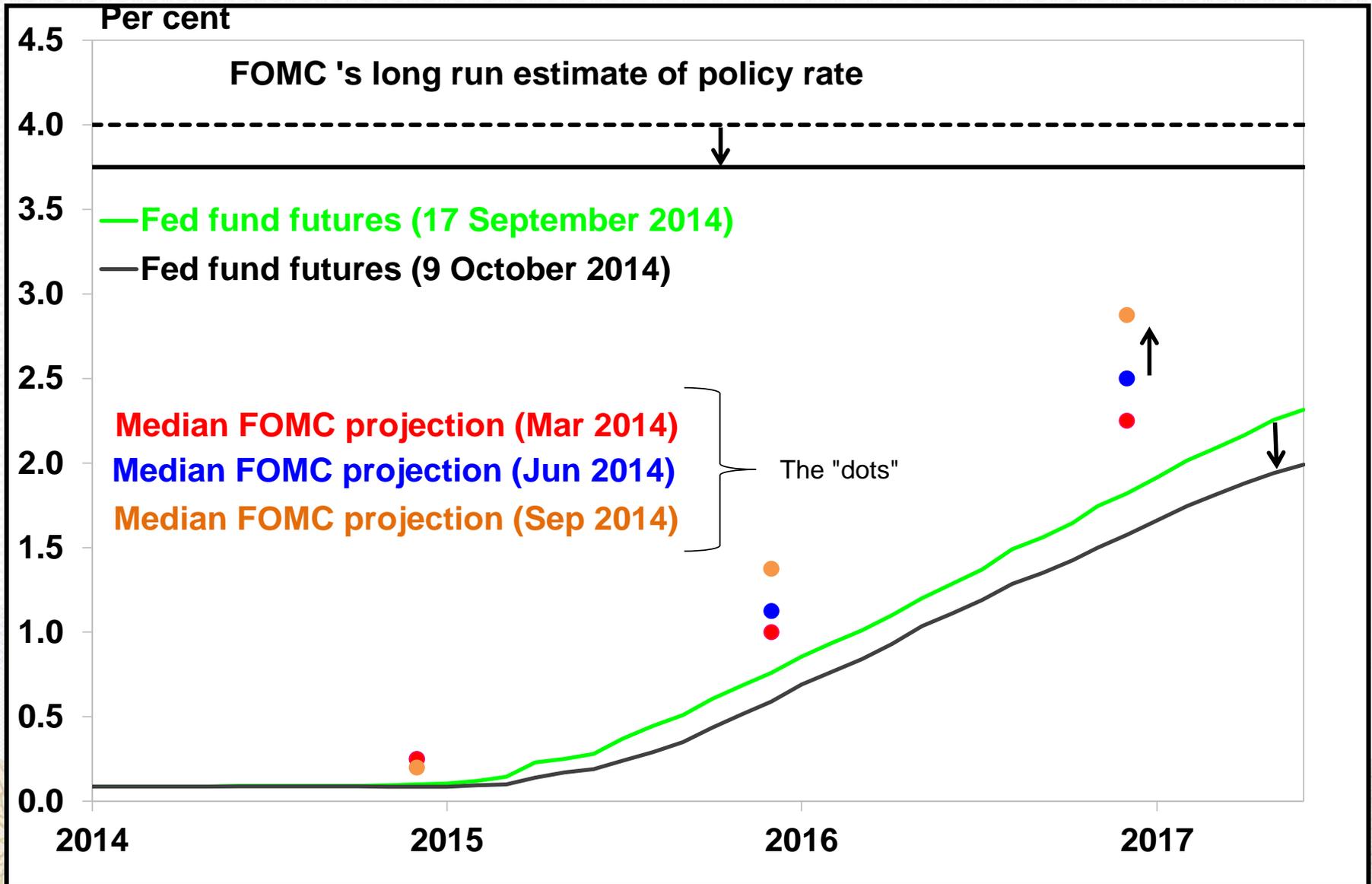
## Global growth and contributions from advanced and emerging economies



Seasonally adjusted annualised rates

Sources: National statistical offices, JPMorgan and staff calculations

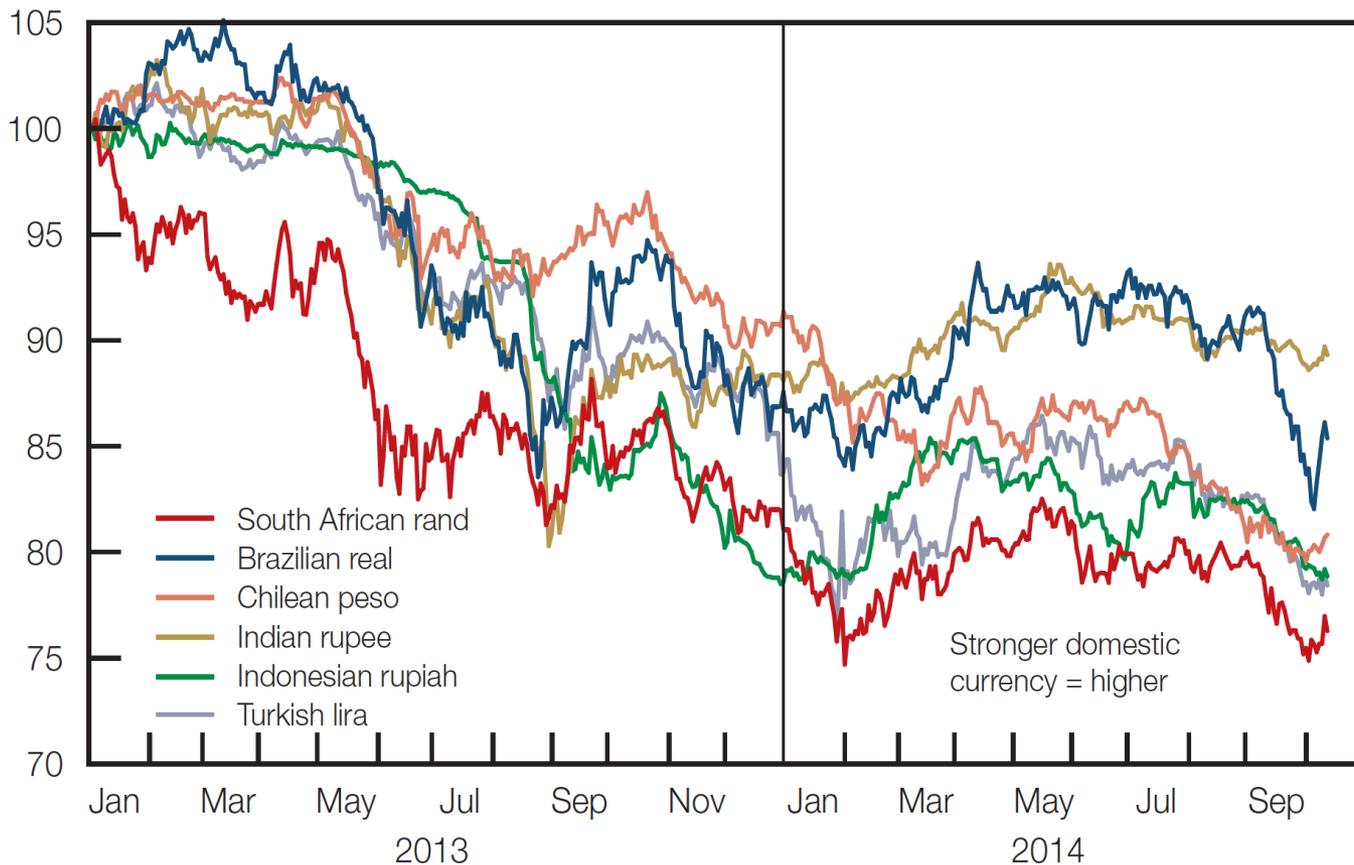
# Expectations of US Fed normalisation are likely to keep changing and impacting on global markets.....



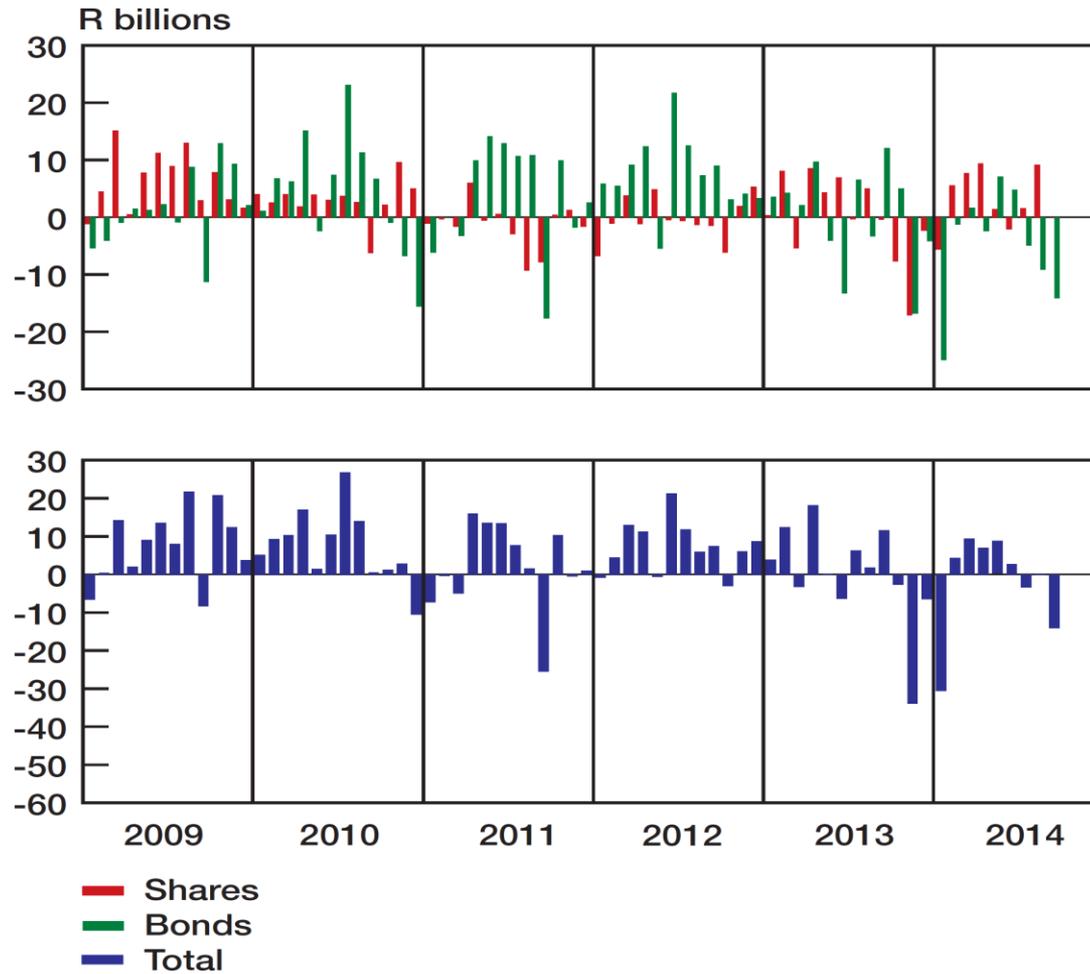
# ...with EM currencies, including the rand sensitive to changing expectations of US policy

## Exchange rates against the US dollar

Indices: 31 December 2012 = 100



# Portfolio flows by non-residents have reflected changes in these perceptions of US policy....

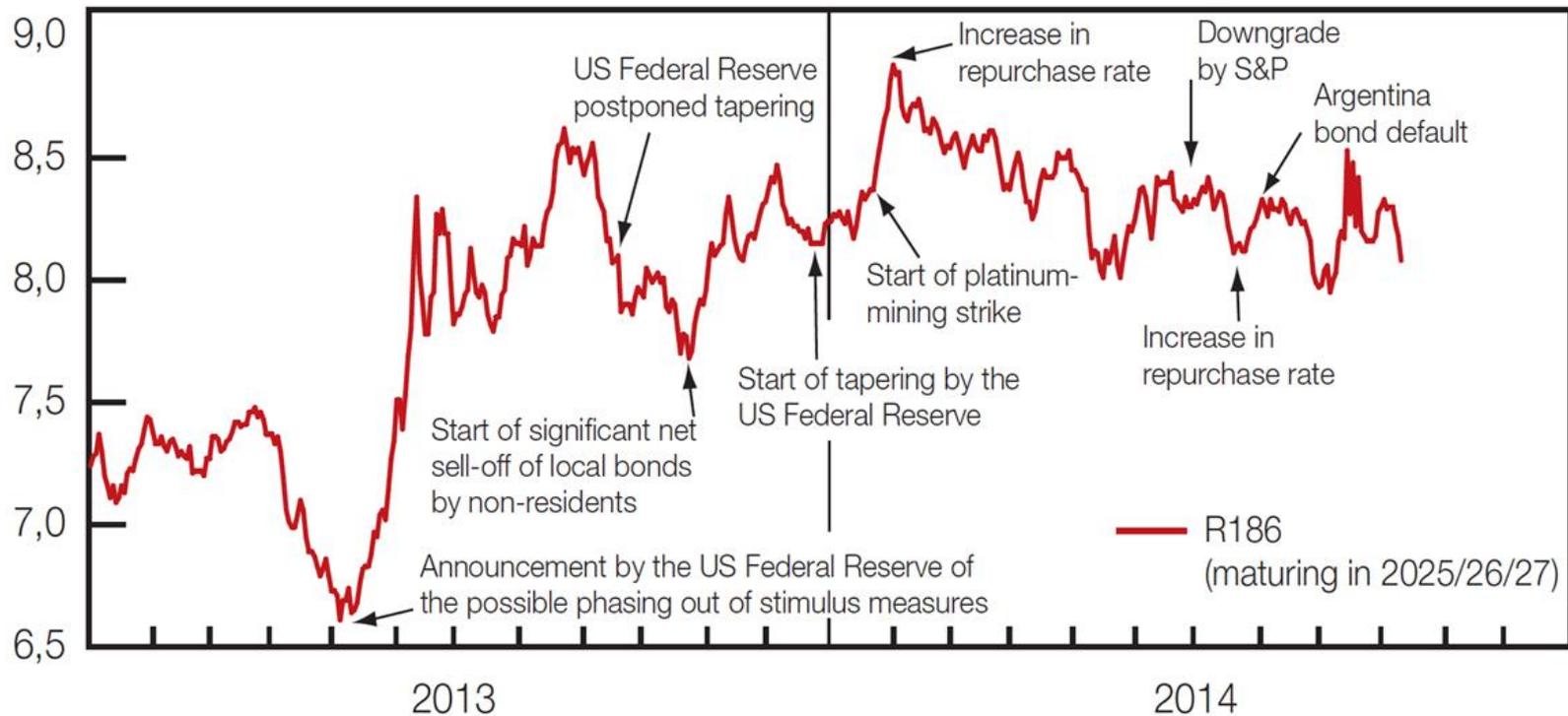


Source: JSE Limited

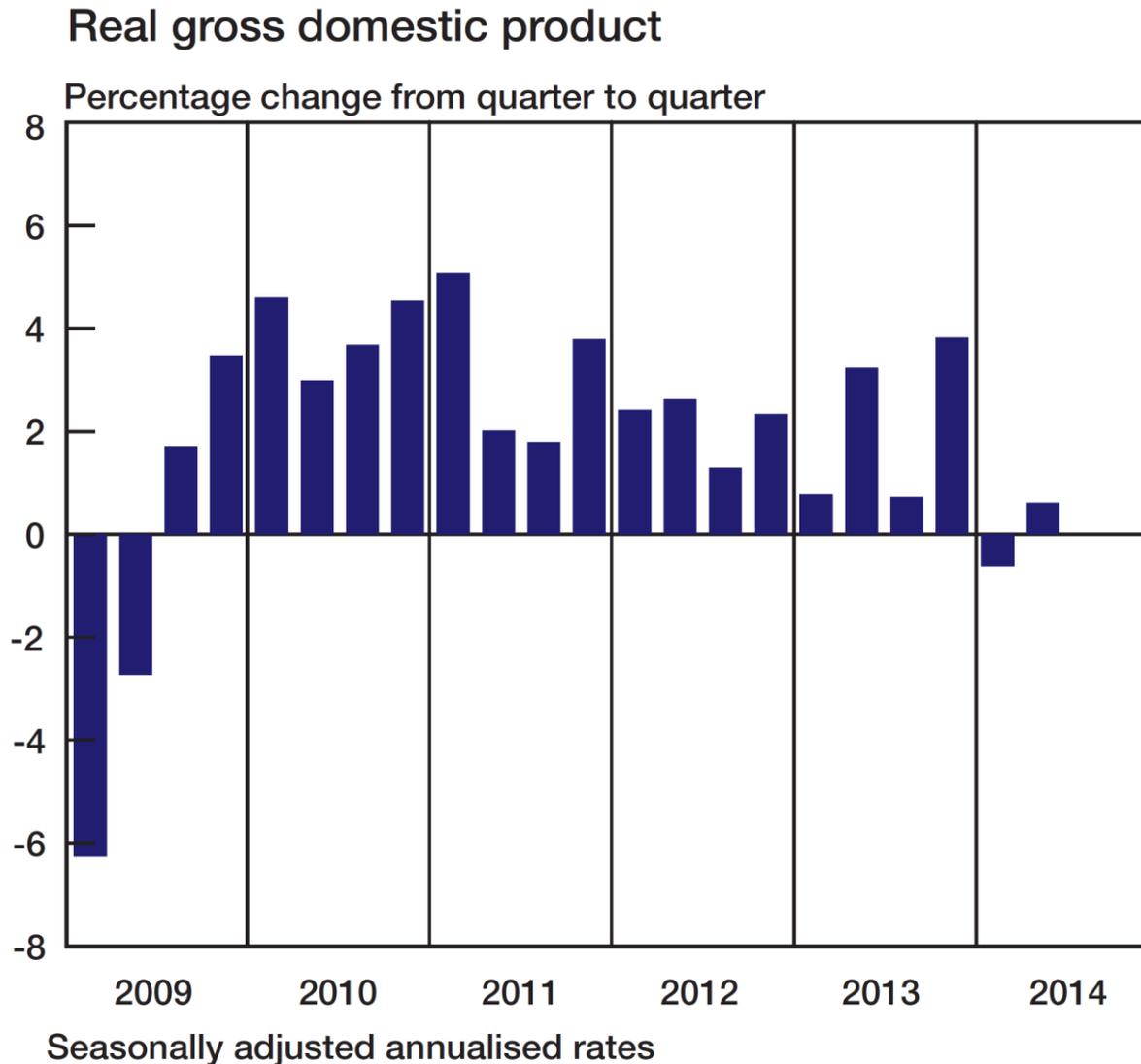
# ..and domestic bond yields also reacted to global and domestic developments

## Government bond yield

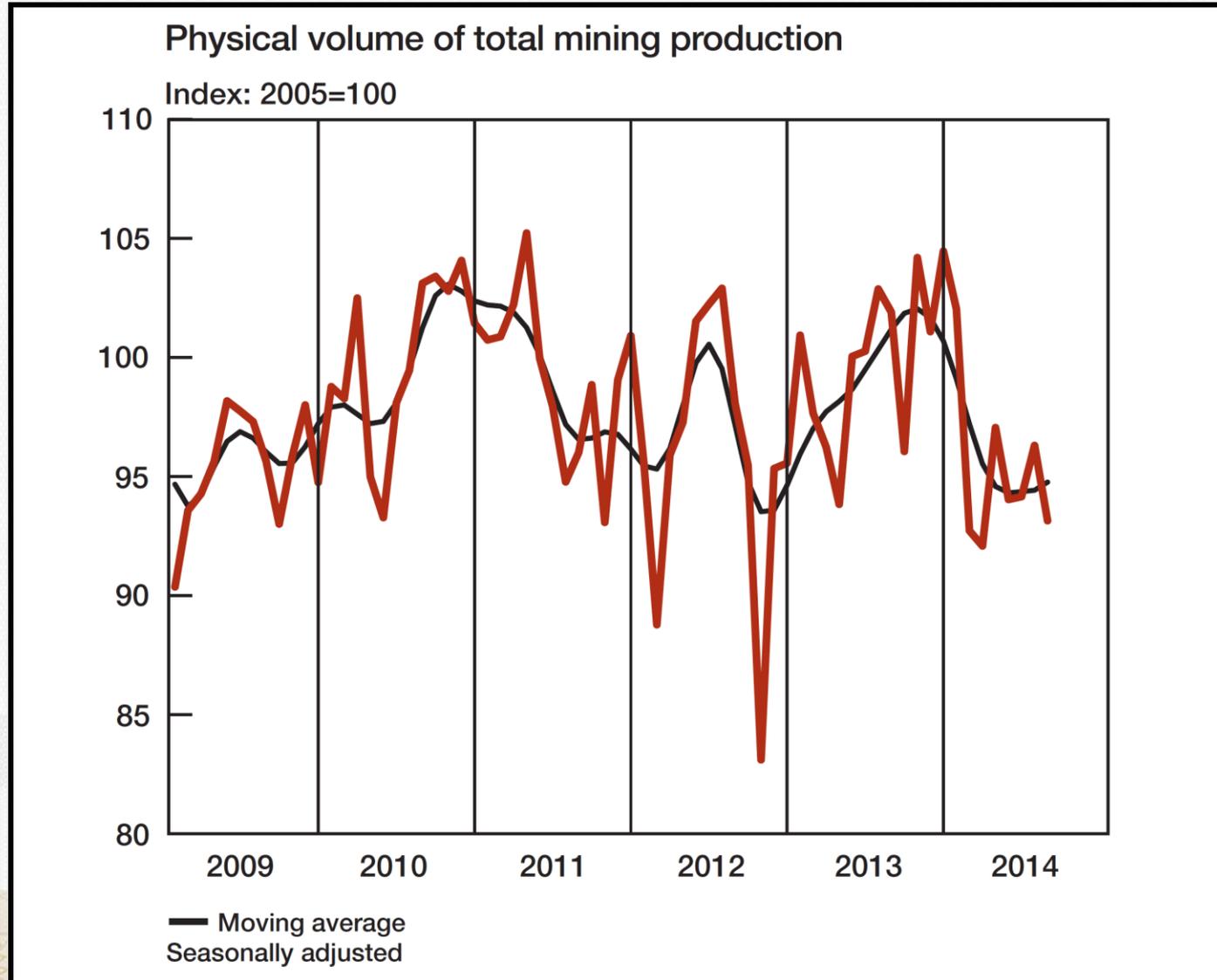
Per cent



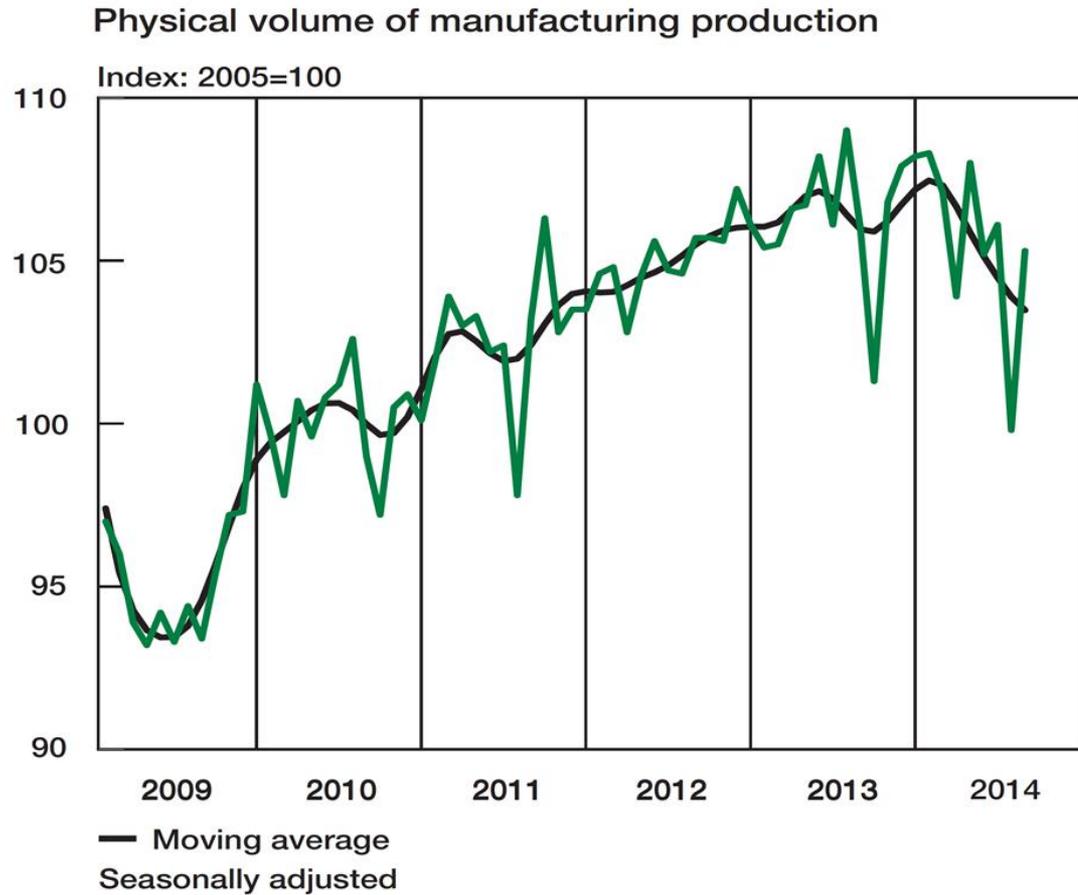
# Domestic growth remains weak despite a return to positive growth in the second quarter....



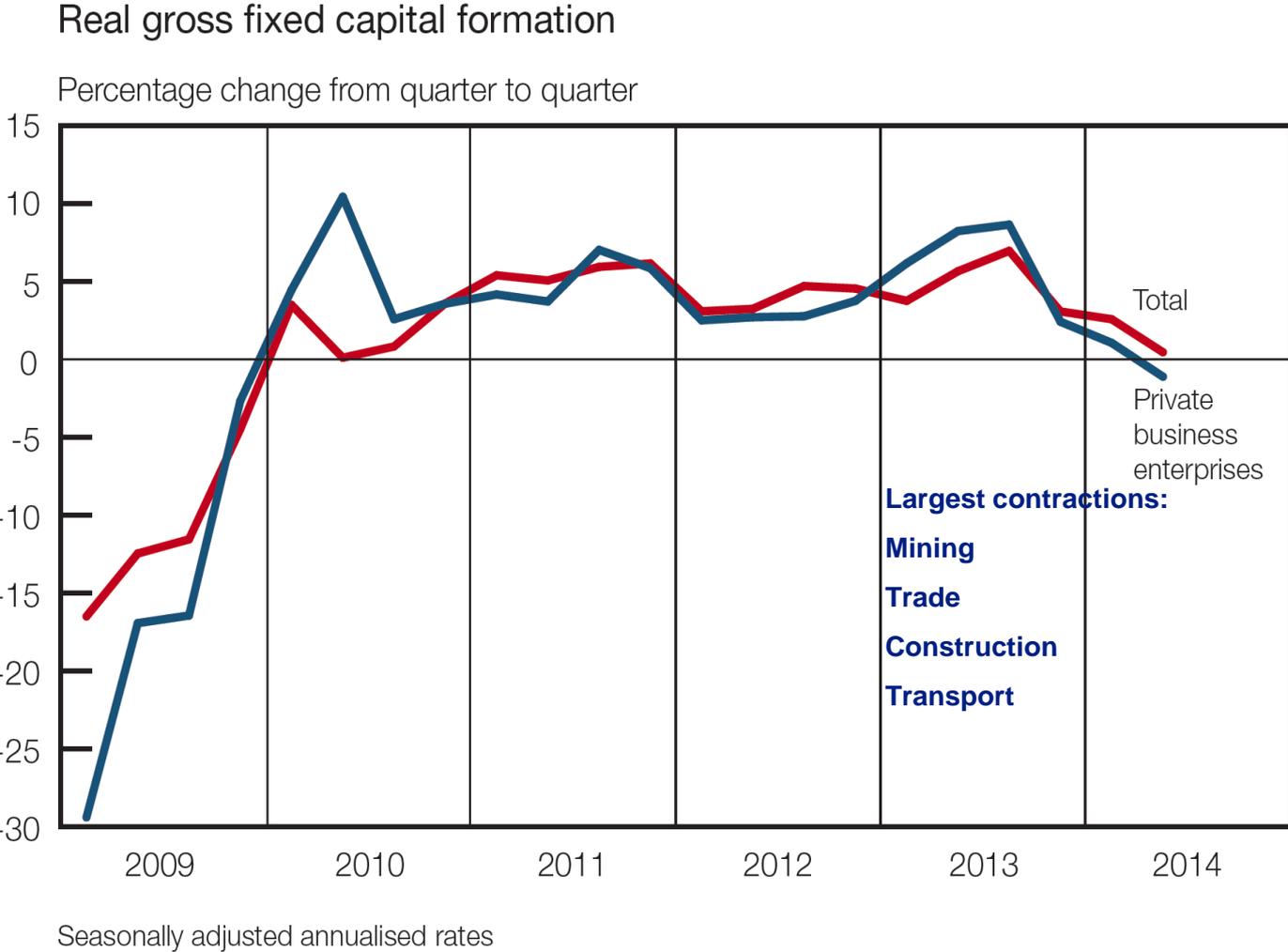
# Mining output continues to decline despite the end to the five-month platinum strike....



... and the manufacturing sector also contracted in the first half of the year



# Real fixed capital formation by the private sector registered a contraction for the first time since 2009



## The Bank's GDP growth forecasts:

- 2014: 1,5 per cent (3,0 per cent in November 2013.....)
- 2015: 2,8 per cent
- 2016: 3,1 per cent
- But risks to the downside
- Continuous downward revisions



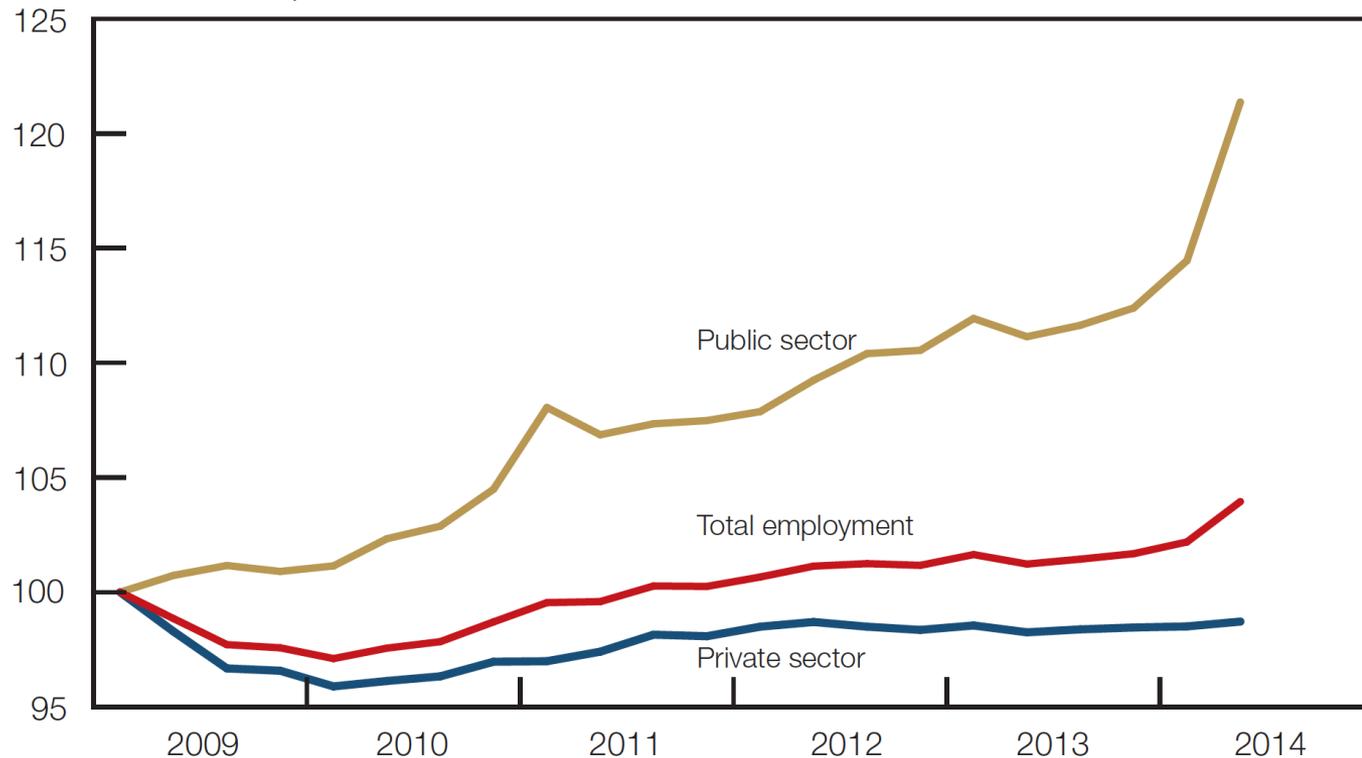
# The unemployment rate has fluctuated around the 25 per cent level for some time....



...and employment in the private sector has not yet recovered to 2008 levels...

### Employment in the formal non-agricultural sector

Indices: First quarter of 2009 = 100

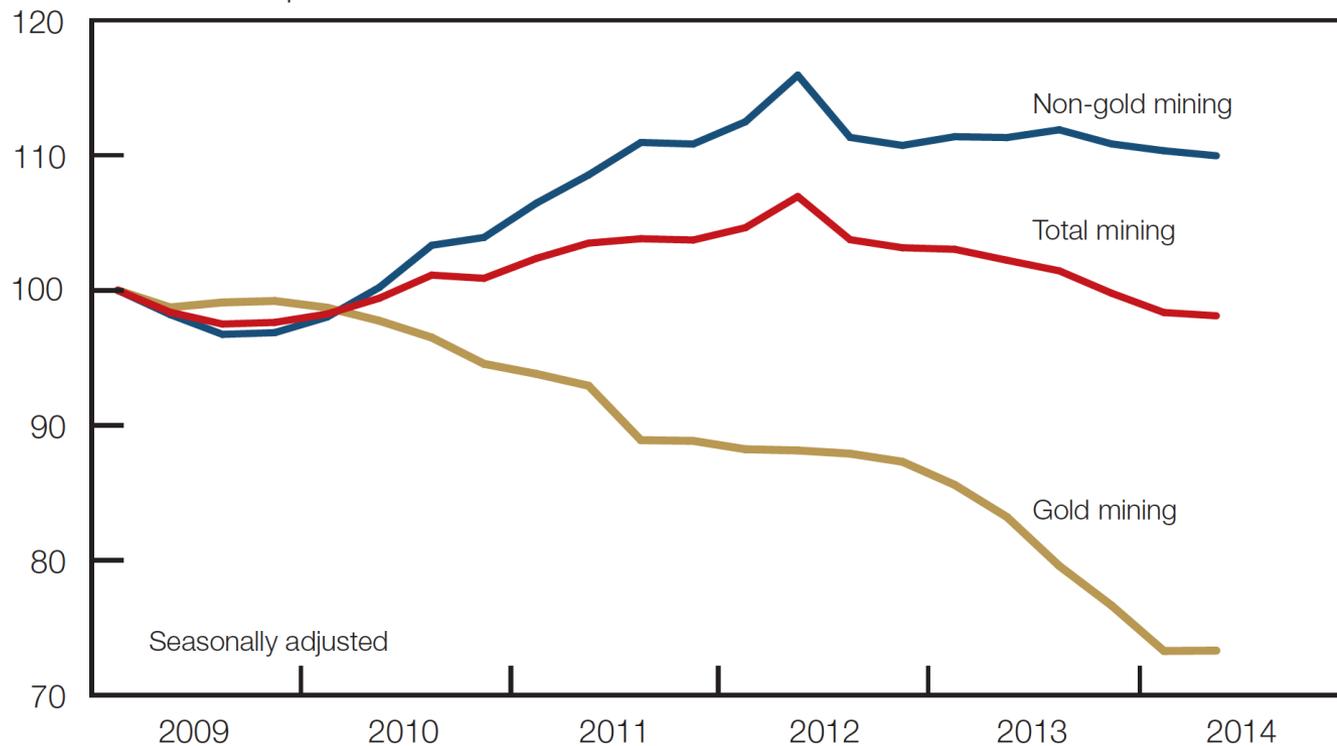


Seasonally adjusted

...with the mining sector in particular employing fewer people...

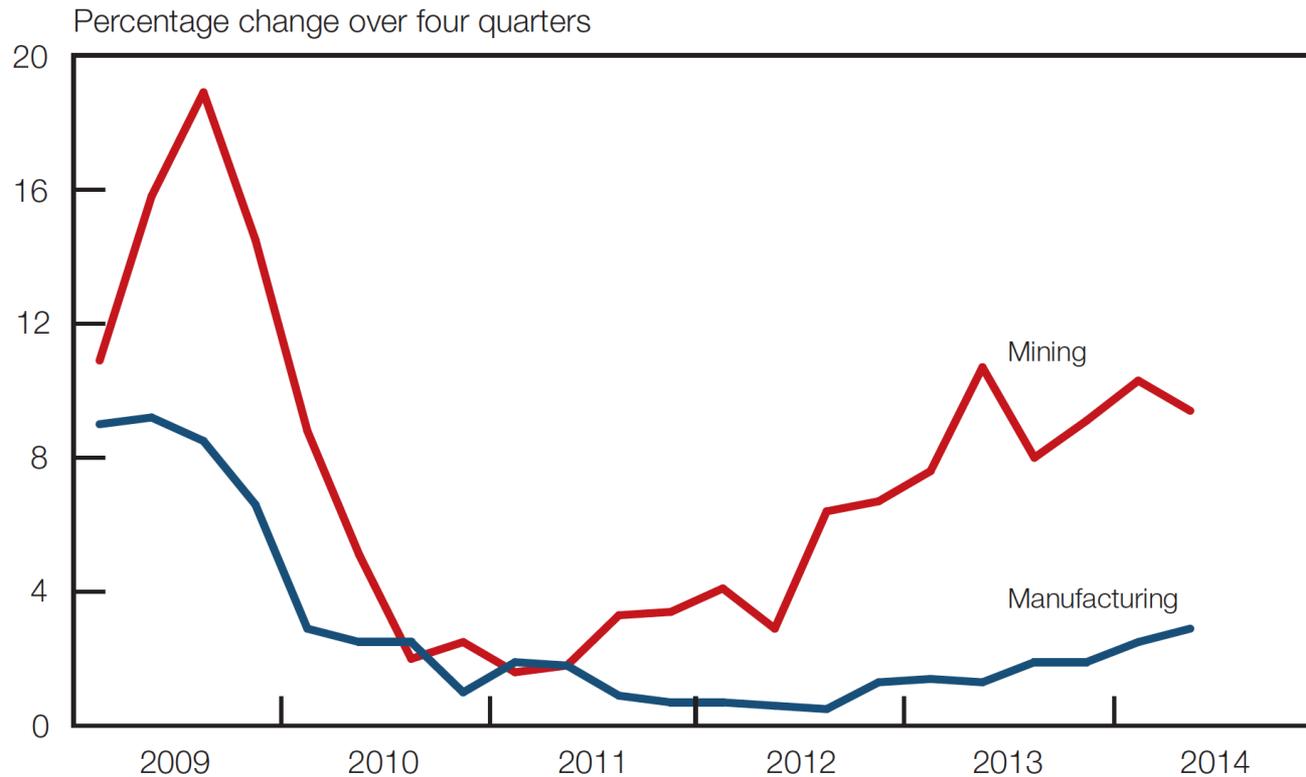
### Mining-sector employment

Indices: First quarter of 2009 = 100



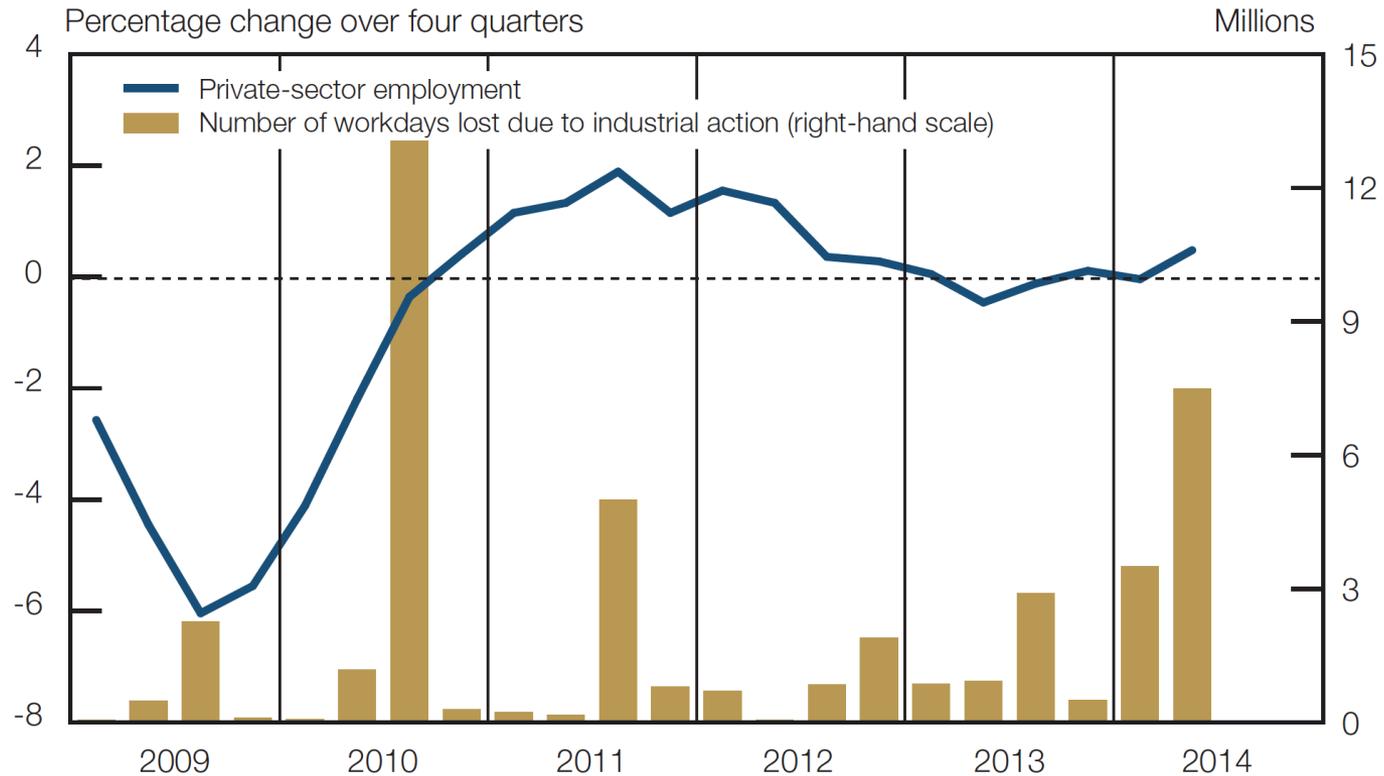
# ...and the capital intensity of production trending higher

Capital-labour ratio in mining and manufacturing



# A significant number of workdays were lost to industrial action in the first half of 2014

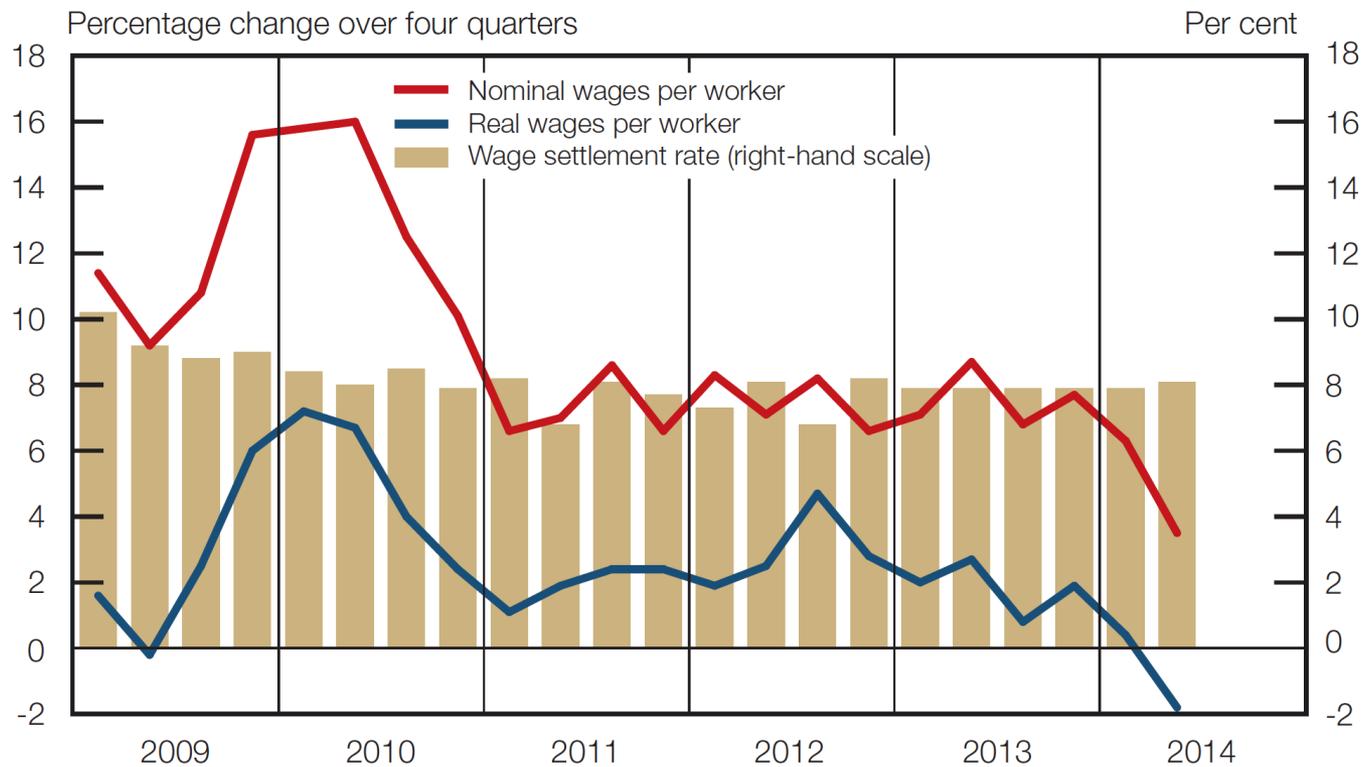
Private-sector employment growth and number of workdays lost due to industrial action



Source: Andrew Levy Employment Publications

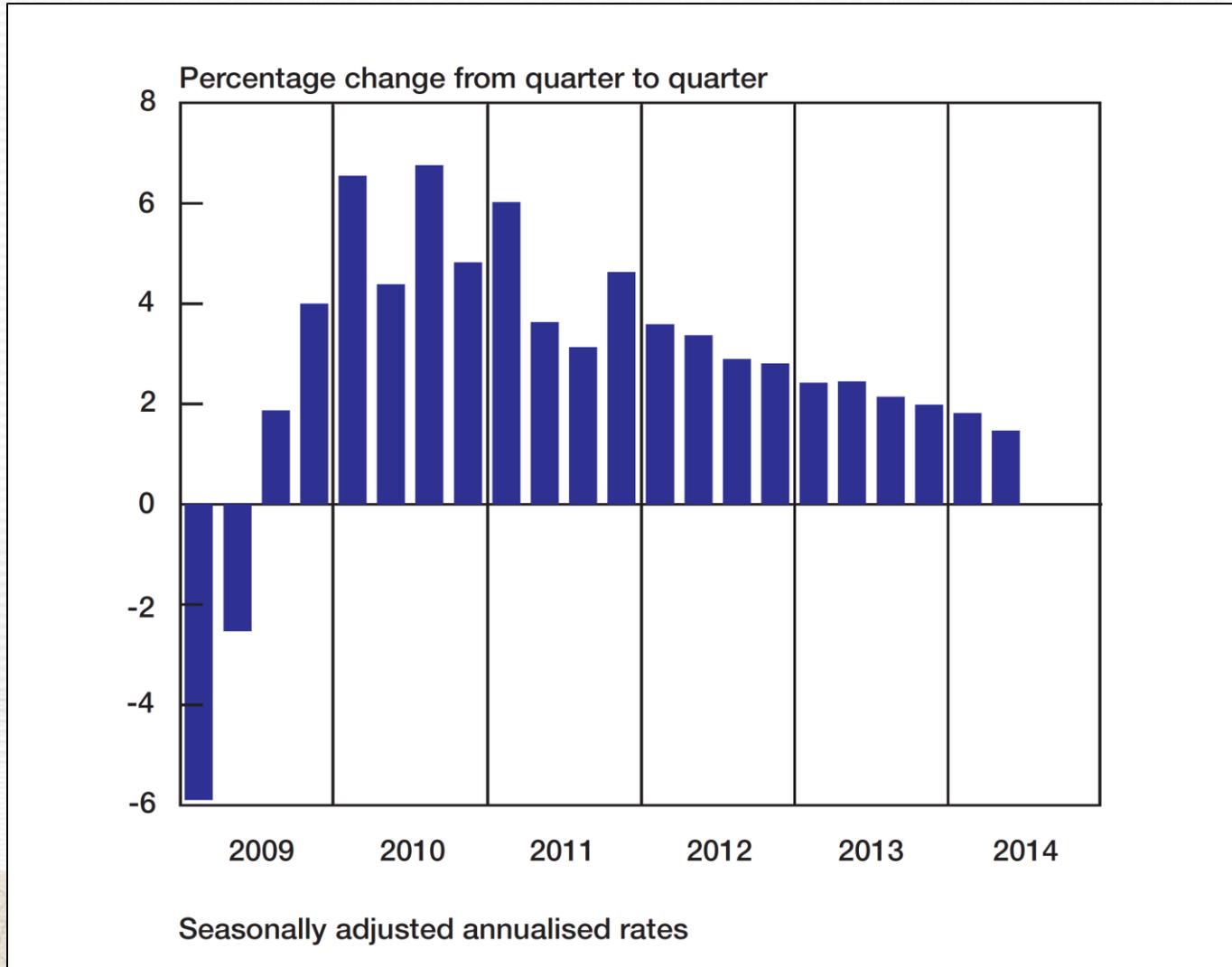
# The strikes resulted in lower wages per worker in Q1 of 2014 as no-work-no-pay pulled remuneration down

Remuneration growth and wage settlement rates\*

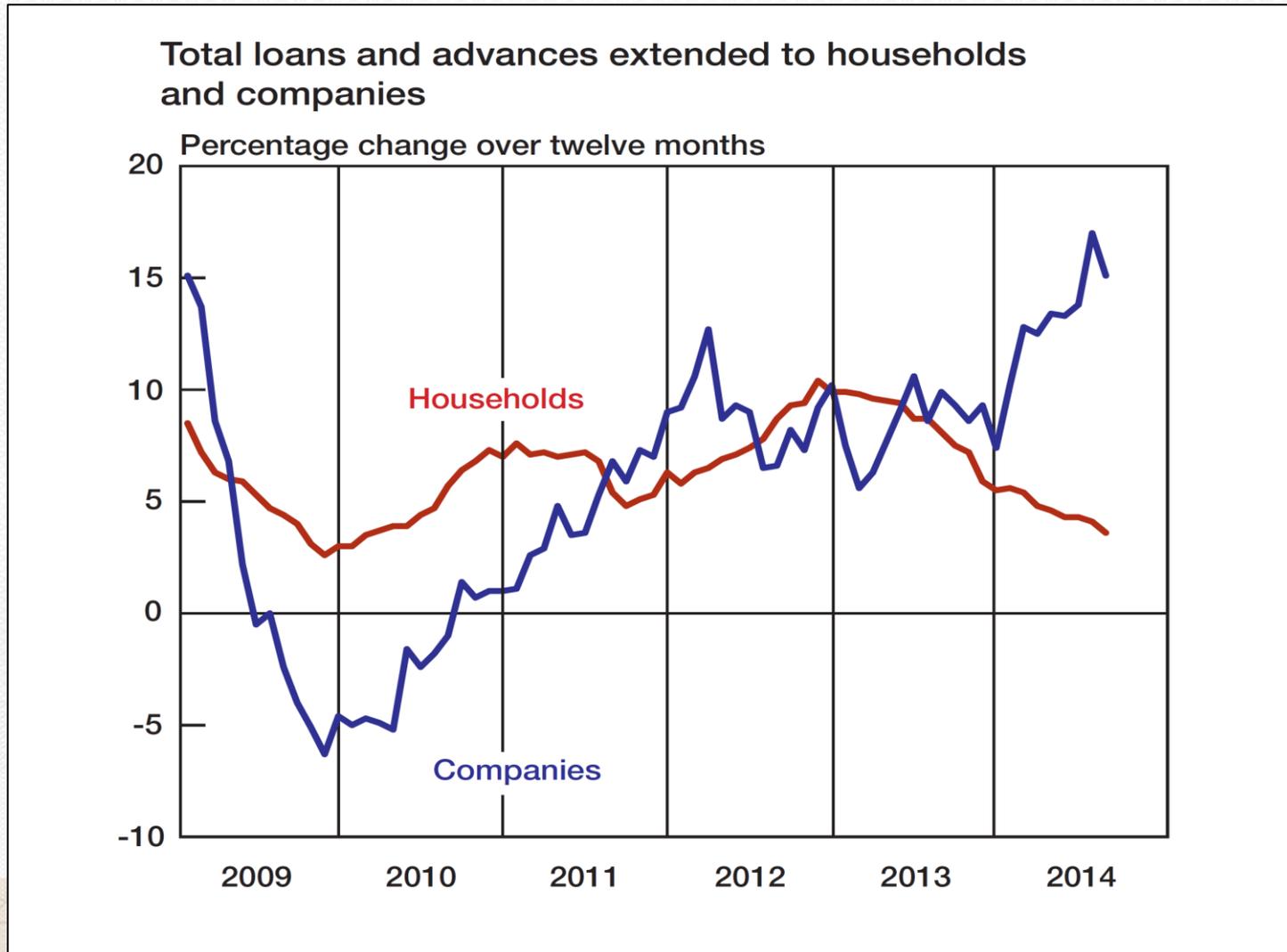


\* Quarterly estimates based on cumulative data provided by Andrew Levy Employment Publications

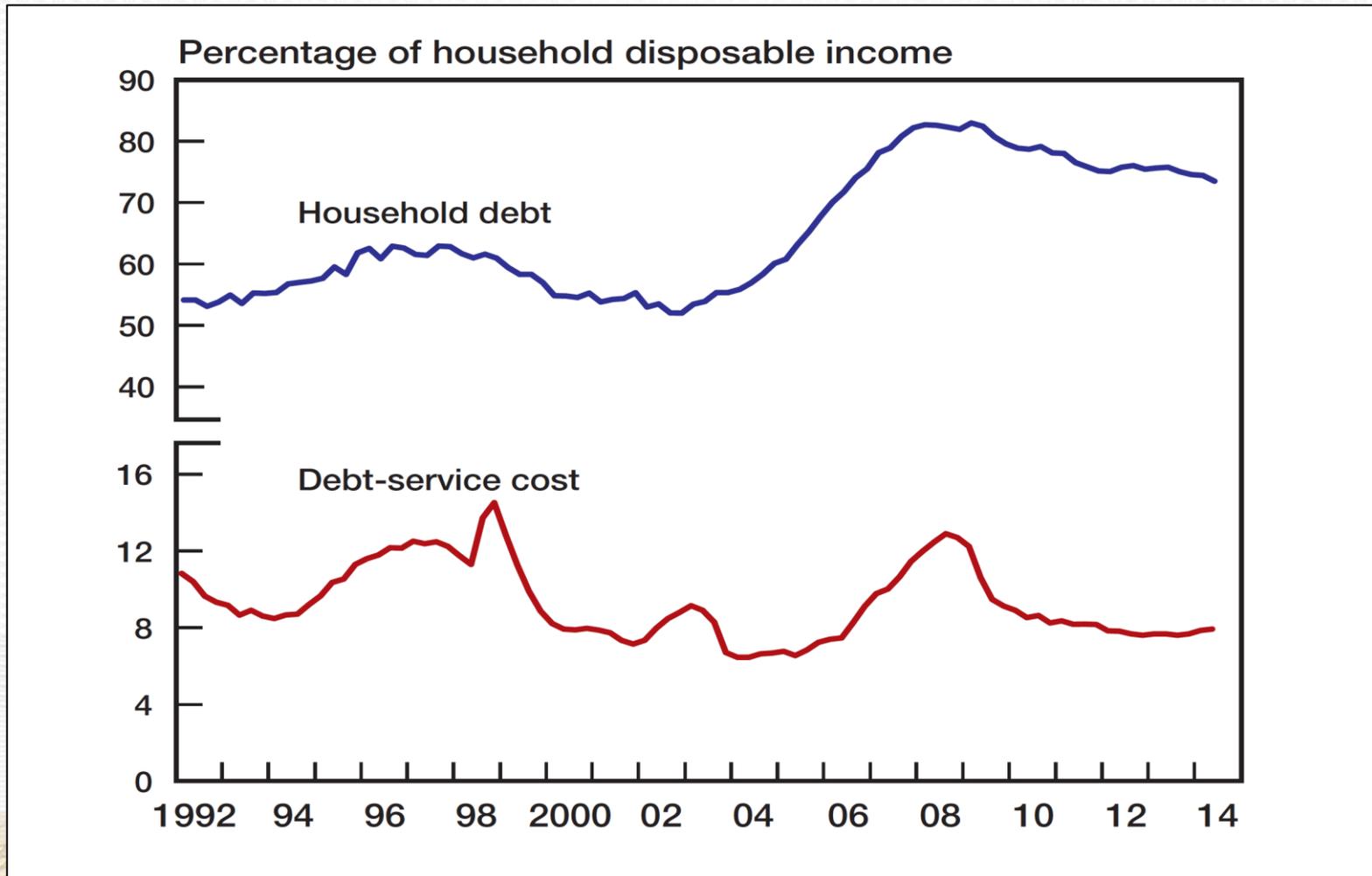
# Growth in household consumption expenditure has been declining steadily.....



...reinforced by increasingly subdued credit extension by banks to households in particular

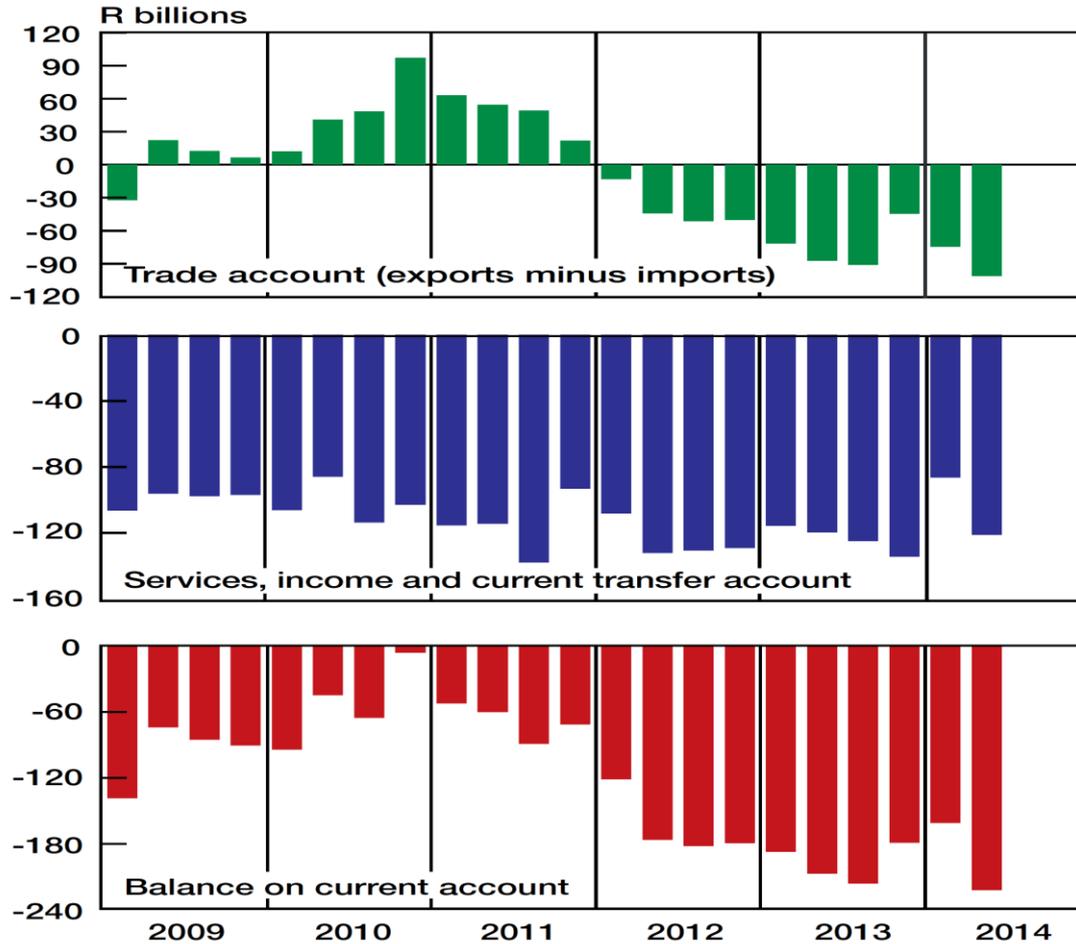


# Household debt remains high, but some gradual deleveraging is evident



# The deficit on the current account widened again in the second quarter of 2014

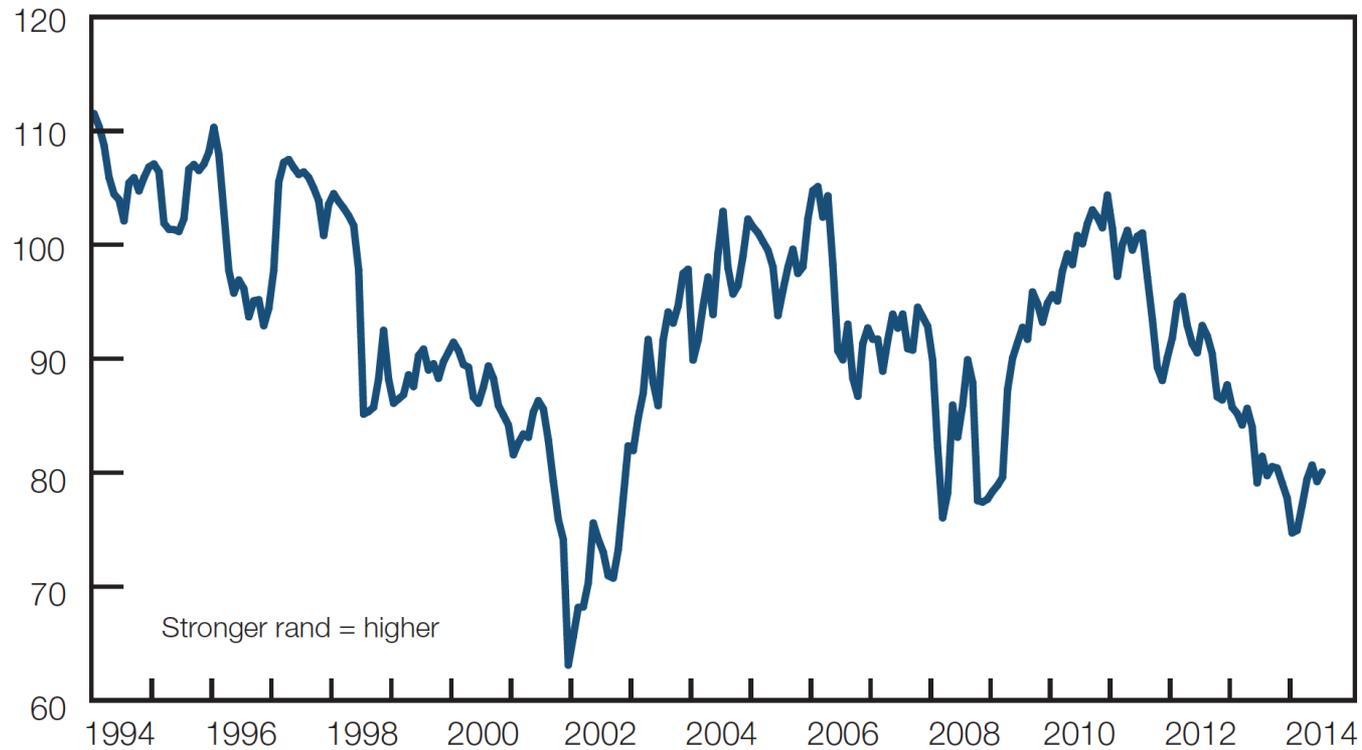
## Balance of payments: Current account



## ...despite a depreciated real exchange rate

Real effective exchange rate of the rand

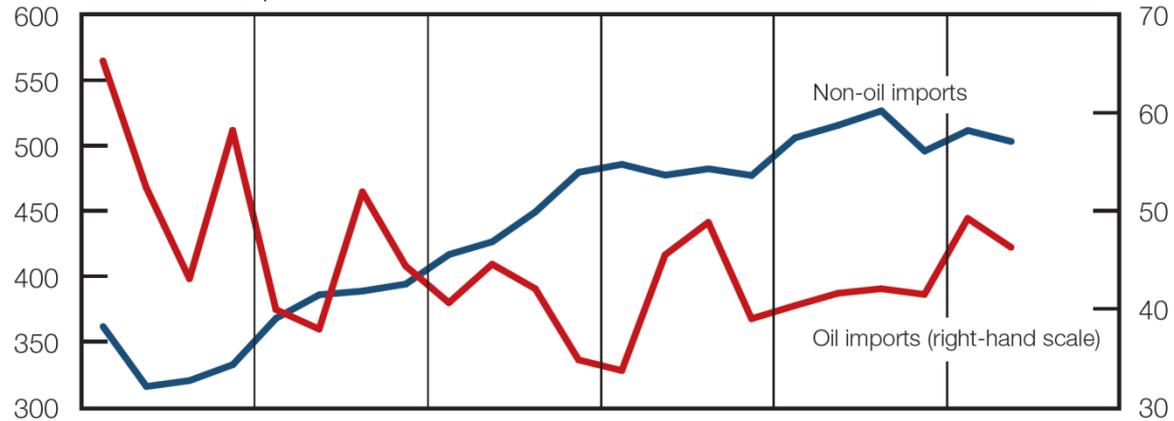
Index: 2010 = 100



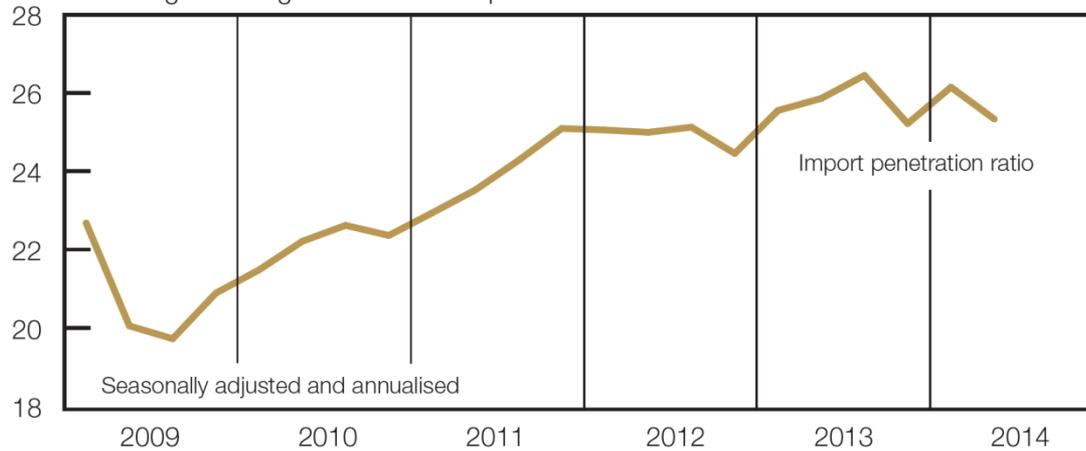
# Imports have not responded strongly to the depreciated exchange rate.....

## Real merchandise imports

R billions, 2005 prices



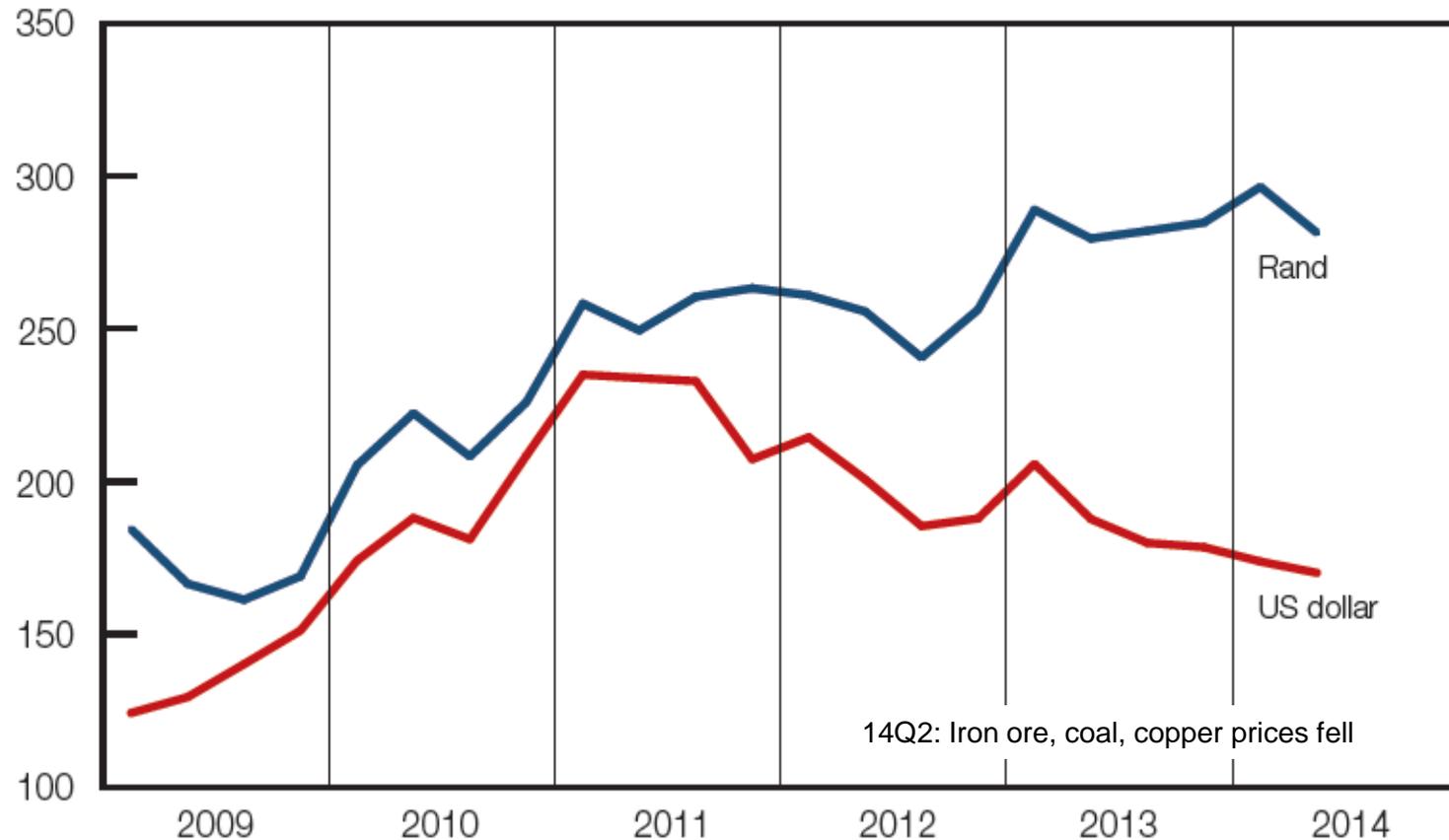
## Percentage of real gross domestic expenditure



## ...and lower prices of export commodities have detracted from export revenue

South African export commodity prices

Indices: 2005 = 100

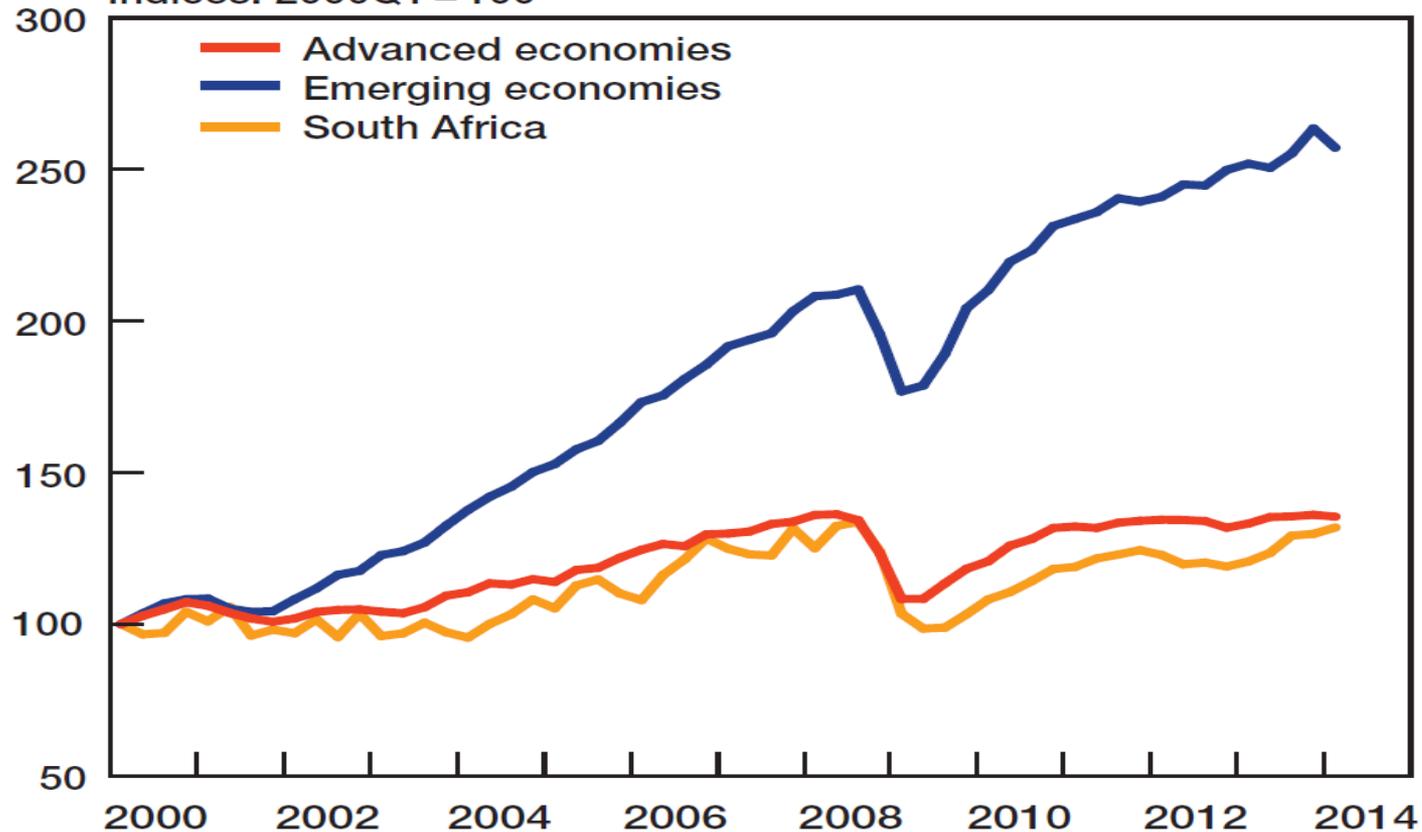


14Q2: Iron ore, coal, copper prices fell

# South African export volume growth has been weak over time, reflecting a loss of competitiveness

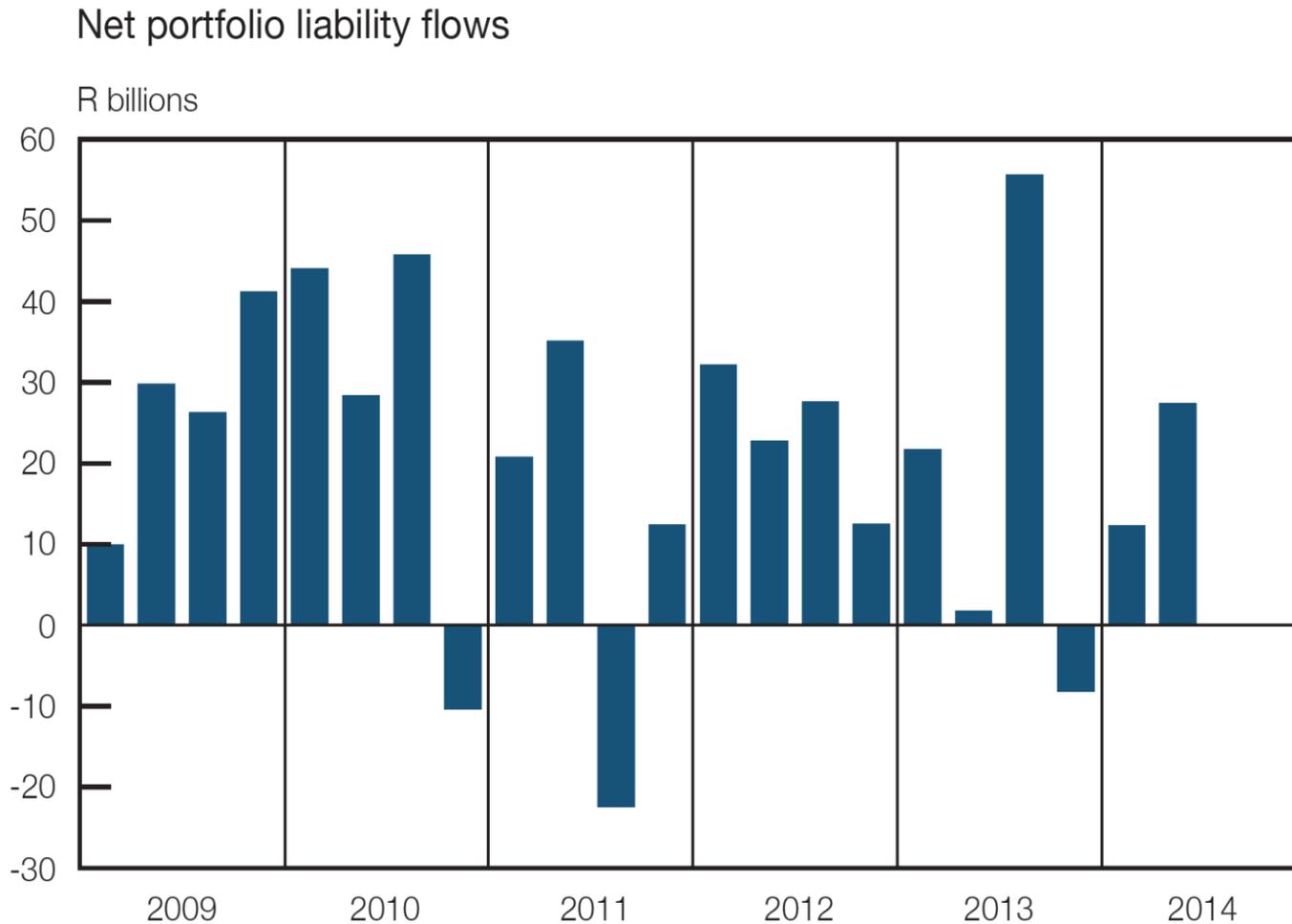
Merchandise export volumes: Advanced economies, emerging economies and South Africa

Indices: 2000Q1 = 100



Source: CPB Netherland Bureau for Economic Policy Analysis, SARB and staff calculations

# Although South Africa attracted further financial inflows from abroad to finance the deficit....



# ....possible sovereign debt ratings downgrades will impact on the cost of financing the deficit

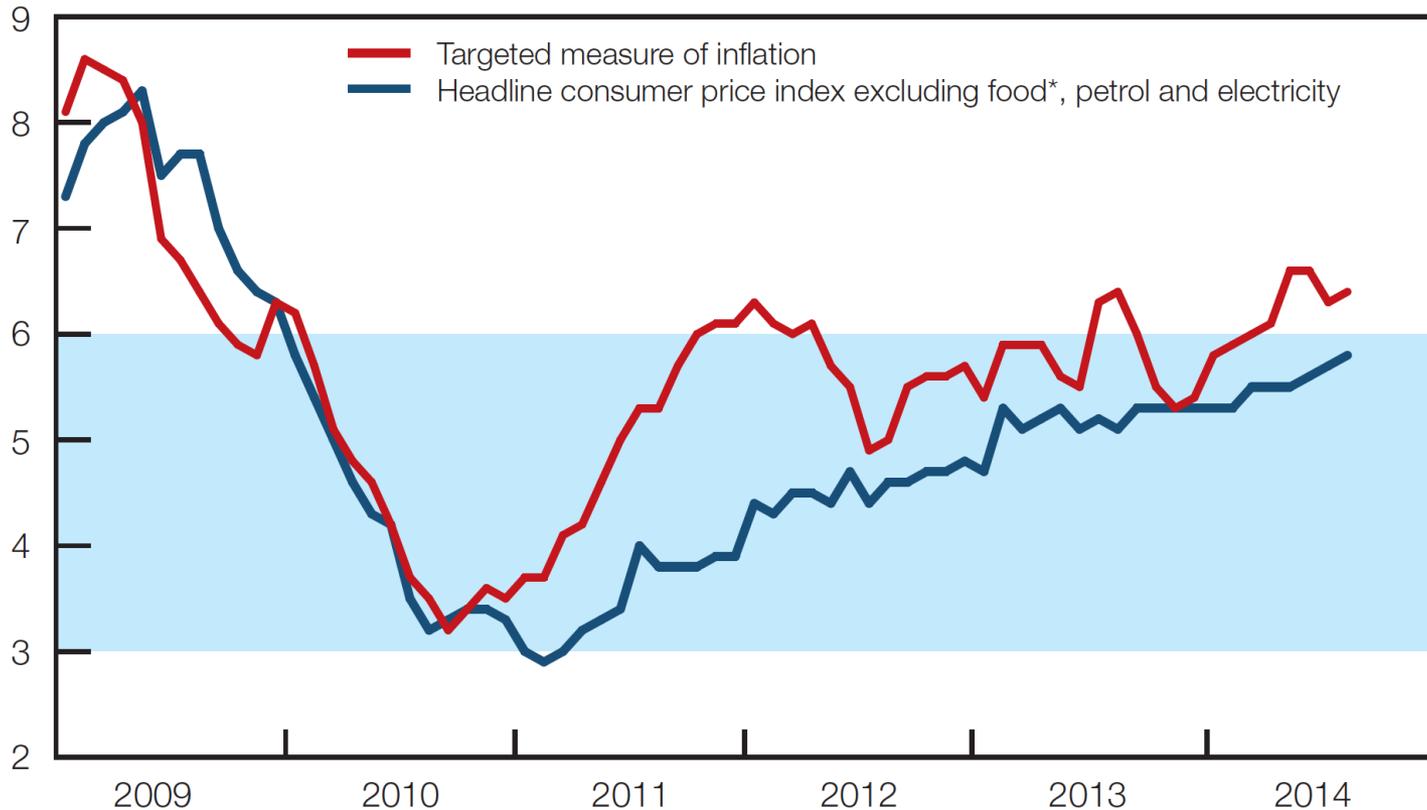
Average yield on US dollar-denominated sovereign bonds by rating category, 20 August 2014

Standard & Poor's rating	Average yield Per cent*	Remarks
BBB+ .....	3,78	Investment grade
BBB .....	3,88	Investment grade
BBB- .....	4,07	Lowest investment grade. South Africa currently falls in this rating category
BB+ .....	4,33	Highest speculative grade
BB .....	4,77	Speculative grade

# Domestic inflation environment is a challenge for monetary policy with rising headline and core inflation

## Underlying measures of consumer price inflation

Percentage change over twelve months

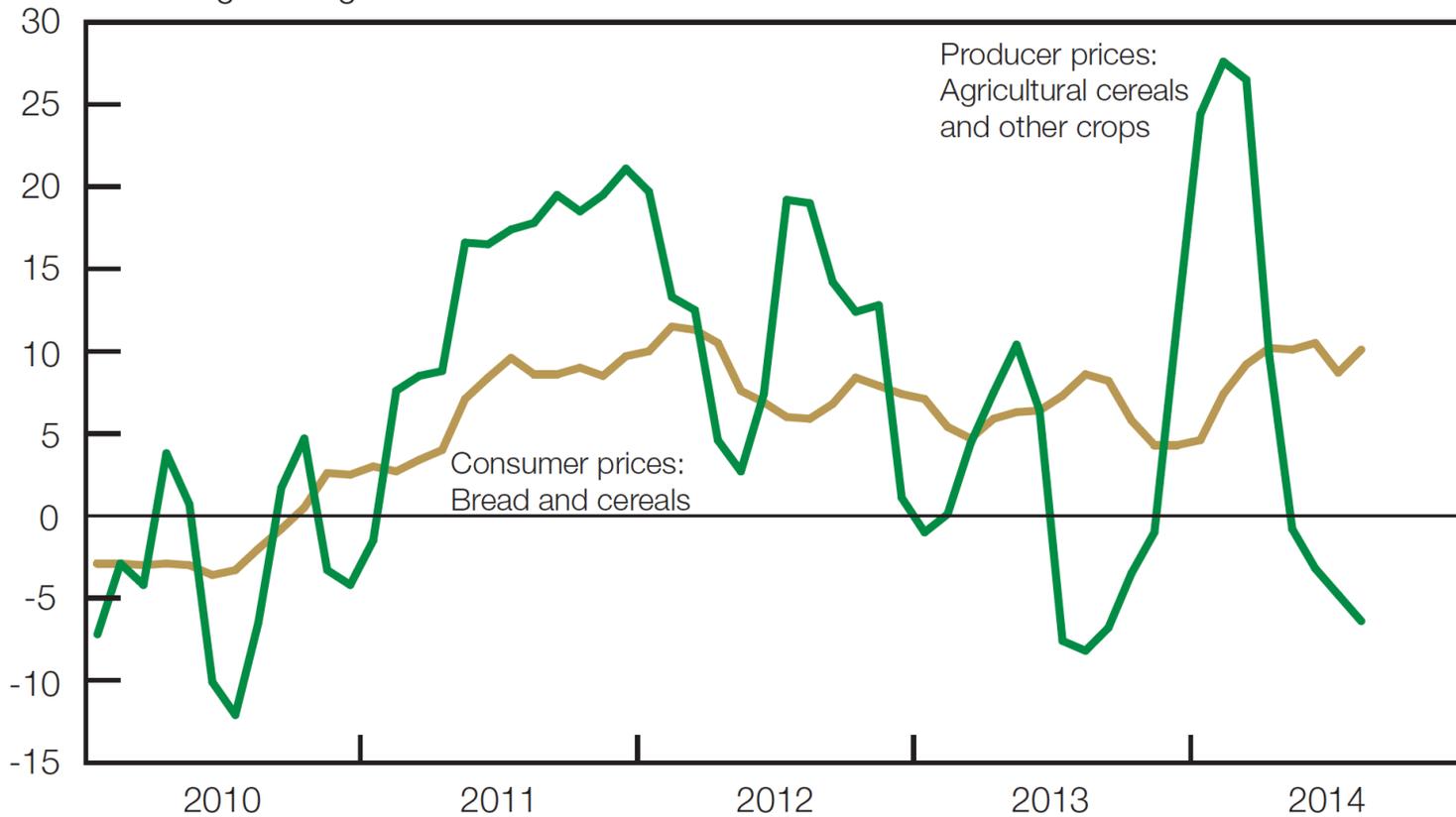


\* Food includes non-alcoholic beverages

# However, lower crop prices are expected to moderate consumer food price inflation....

## Producer and consumer food price inflation

Percentage change over twelve months

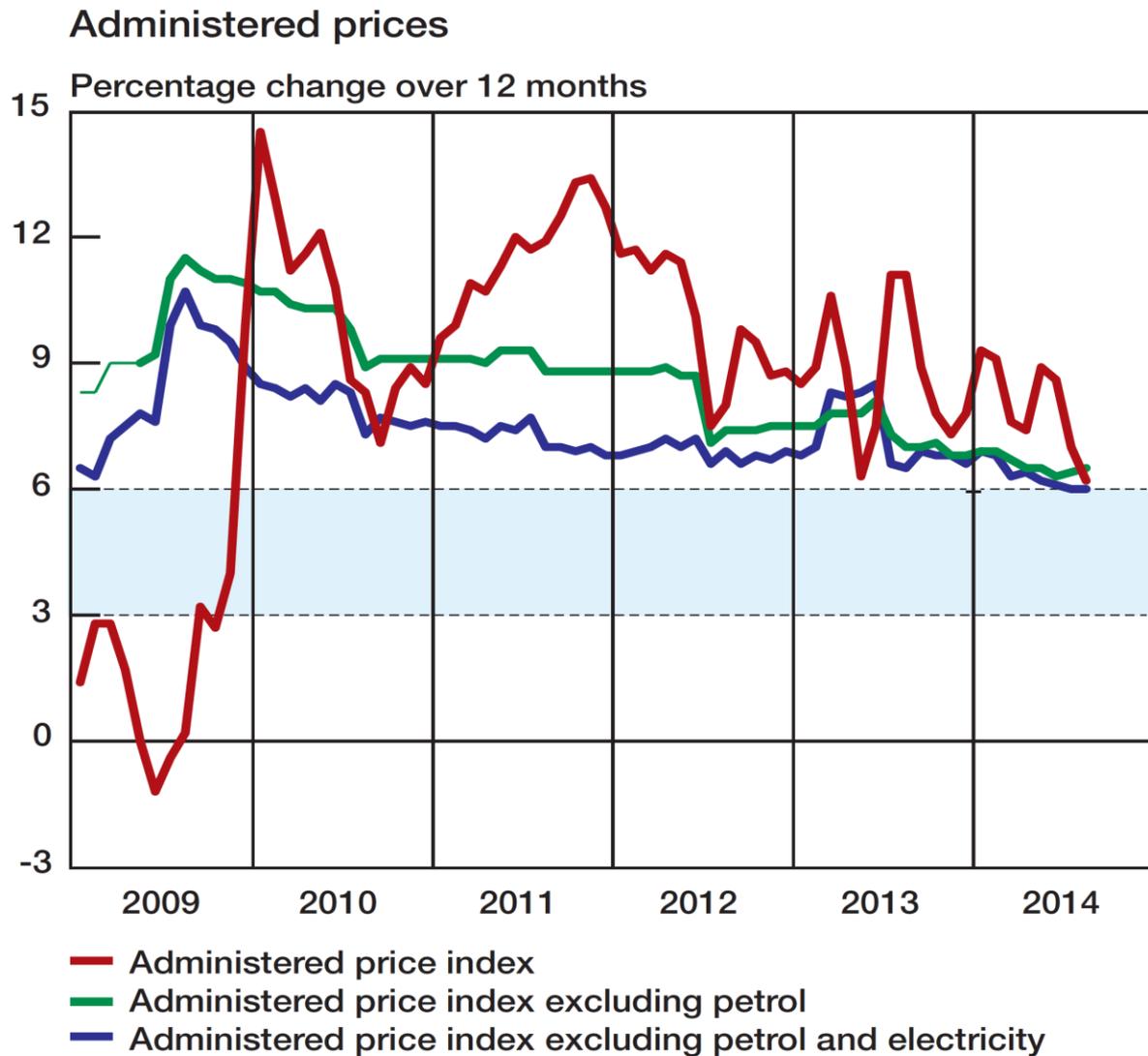


....and pressures from international oil prices have moderated recently

## International crude oil prices



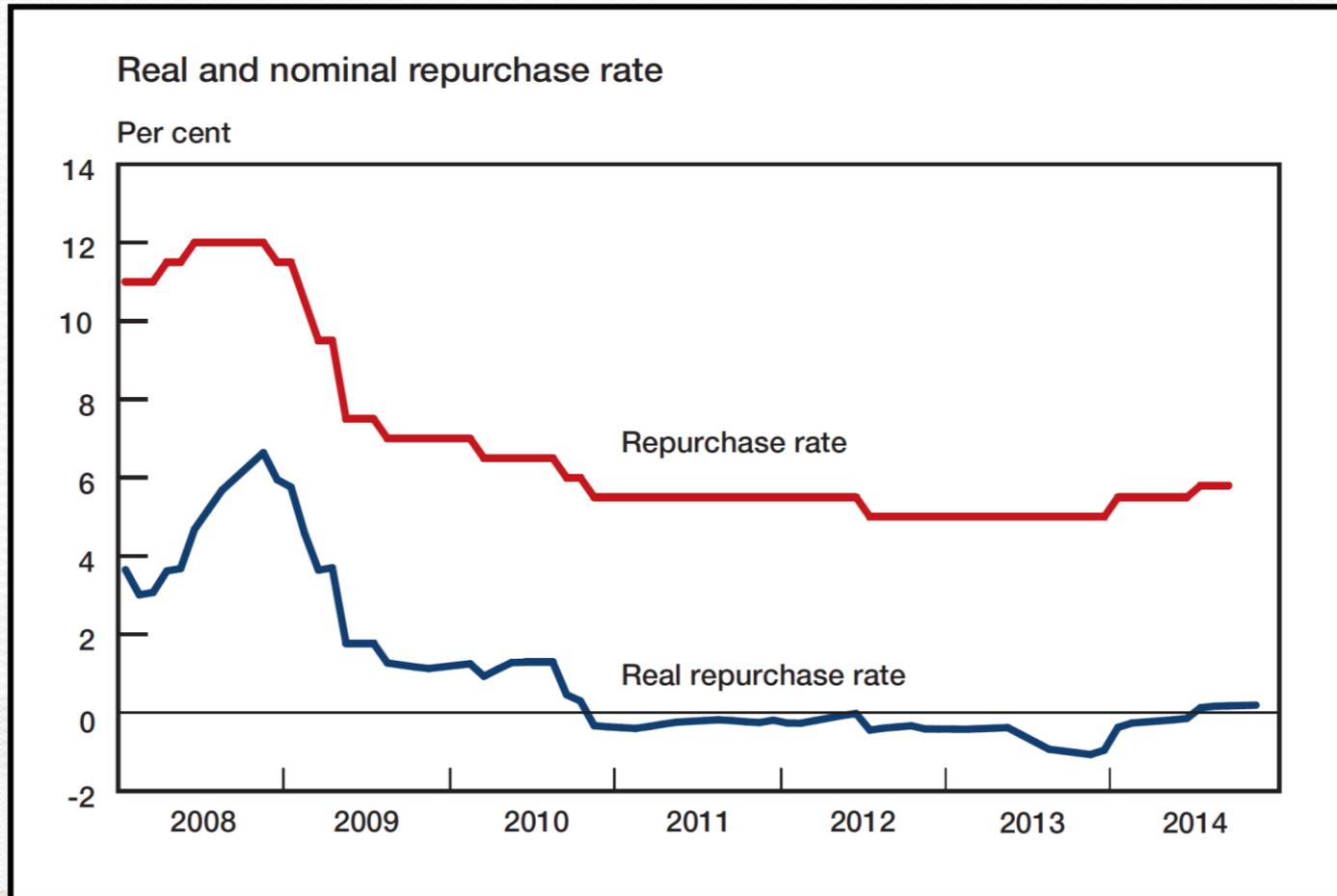
# Administered prices remain above the upper end of the target range



## Inflation forecast: some moderation expected with risks assessed to be on the upside, mainly from the exchange rate and wage pressures

- **Headline:**
- 2014: average 6,2 per cent
- Peak of 6,5 per cent in Q2
  
- 2015: average 5,7 per cent
- To return to within the target range in Q1
  
- 2016: average 5,8 per cent.
  
- **Core:**
- 2014: 5,6 per cent
- 2015: 5,7 per cent
- 2016: 5,5 per cent

Monetary policy has responded to higher inflation pressures, but has been sensitive to the real economy, with the real repo rate only slightly positive



Nominal repurchase rate adjusted with 12-month ahead Reuters consensus expectations

# Group Annual Financial Statements



# SARB Group

The SARB Group (The Group) consists of the Bank and four wholly-owned subsidiaries.

➤ **The Corporation for Public Deposits (CPD)**

- Governed by the CPD Act
- Accepts call deposits from the public sector and invests in short term money market instruments
- Has an independent Board, appointed by the Minister of Finance
- Surplus profits are transferred to Government

➤ **South African Bank Note Company (SABN)**

- Registered in terms of the Companies Act
- Produces banknotes
- Has an independent Board and sub-committees

## SARB Group (continued ...)

### ➤ **South African Mint Company (SA Mint)**

- Registered in terms of the Companies Act
- Produces coin
- Has an independent Board and sub-committees

### **South African Reserve Bank Captive Insurance Company (SARBCIC)**

- Registered in terms of the Companies Act as a public company
- SARBCIC carries out short-term insurance business for the Bank and its subsidiaries
- Has an independent Board and sub-committees

## Stylized facts

- Rand depreciated over the year from 9.20 to 10.58 causing increases in the gold and foreign exchange, as well as foreign loans and deposits, and the Gold and Foreign Exchange Contingency Reserve (GFECRA).
- Gold price decreased to R13 687 per fine ounce from R14 742 (2013) causing decreases in the gold reserves. Gold holdings increased by 1 192 fine ounces.
- Prestige Bullion (a 60% subsidiary of the SA Mint) numbers were consolidated for the first time – 18 months included in the current Group numbers resulting in a profit for the Group of R92,0 million and a non-controlling interest attributable to Rand Refinery of R88,7 million.



# Summarised Annual Financial Statements

- The summarised Group annual financial statements form part of the annual report as part of the 'integrated reporting journey'.
- Only material balances and notes have been disclosed, together with the full disclosure on accounting policies.
- An audit opinion, directors' report and report of the audit committee are also included.
- Financial framework details the reporting framework of the summarised financial statements.
- The full set of annual financial statements has been prepared as in prior year's - statutory requirement. This is available on the Bank's website.



# Statement of comprehensive income

	Group R'm	
	2014	Restated 2013
Net interest income	1 715	1 629
Other income	1 129	509
Operating costs	(4 685)	(3 910)
<b>Loss before taxation</b>	<b>(1 841)</b>	<b>(1 772)</b>
Taxation	524	522
<b>Loss after taxation</b>	<b>(1 317)</b>	<b>(1 250)</b>
Non-controlling interest	(89)	-
<b>Loss attributable to the parent</b>	<b>(1 406)</b>	<b>(1 250)</b>
<b>Movements through OCI</b>	<b>(309)</b>	<b>(16)</b>
<b>Total comprehensive loss for the year</b>	<b>(1 715)</b>	<b>(1 266)</b>

## Group Results

### ➤ Net interest income

An increase of R86 million from the prior year.

### ➤ Operating costs

Increased by R775 million from last year. The key contributors are :

- Personnel costs increased by R288 million for the SARB, R46 million for the subsidiaries and a restatement of R219 million which relates to the restatement of post-employment benefits for the SARB and SABN;
- Cost of new currency increased by R110 million for the SARB; and
- Other operating costs increased by R141 million for the SARB and R359 million for the subsidiaries.



# Statement of comprehensive income (continued...)

## Group Results

### > Loss attributable to the parent

Current year of R1,4 billion compared to the prior year of R1,3 billion.

The contributors to the Group's net profit are as follows:

	Group	
	R'm	
	2014	2013
CPD	55	98
SA Mint	181	(5)
SABN	47	3
SARBCIC	6	(2)
Subsidiaries' profit contribution	289	94
Bank's net loss after taxation	(1 606)	(1 344)
Group loss after taxation	(1 317)	(1 250)
Non-controlling interest *	(89)	0
<b>Total loss attributable to the parent</b>	<b>(1 406)</b>	<b>(1 250)</b>

\* non -controlling interest of 40% held in Prestige Bullion, attributable to Rand Refinery



# Statement of financial position

	Group R'm	
	2014	Restated 2013
Total assets	600 889	532 015
Total liabilities	594 502	523 889
Total capital and reserves	6 387	8 126
USD / ZAR exchange rate	10,58	9,20
Gold price, per fine ounce	R13 687	R14 742

➤ **Total assets of the Group increased by R68,9 billion**

Gold and foreign exchange increased by R63,2 billion – R67,4 billion increase due to the depreciation of the rand offset by a decrease of R4,2 billion due to the gold price decrease.

➤ **Total liabilities of the Group increased by R70,6 billion**

GFECRA increased by R52,4 billion due to the depreciation of the rand offset by the decrease in the gold price. Deposit accounts increased by R13,3 billion largely due to the depreciation of the rand. Likewise foreign loans and deposits increased by R4 billion.

➤ **Contingency reserve of the Group decreased by R1,6 billion**

Loss of R1,6 billion decreased the reserve, which amounted to R4,7 billion at the reporting date.



# Conclusions

- A somewhat improved global growth picture in 2014Q2, but emerging risks
- Weak economic growth outlook for South Africa
- Inflation above target, with upside risks, resulting in a moderate tightening cycle
- Monetary policy will continue to focus on its inflation mandate, but sensitive to the state of the real economy
- Given the global and domestic economic context and expanded mandate, financial situation continues to be challenging